

MULTIMEDIA



UNIVERSITY

STUDENT ID NO

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MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 2, 2018/2019

BAC3654 – PROFESSIONAL ETHICS

(All sections / Groups)

14 MARCH 2019
9.00 a.m – 12.00 p.m
(3 Hours)

INSTRUCTIONS TO STUDENTS

1. This Question paper consists of 5 pages (excluding cover page) with 4 Questions only.
2. Attempt **ALL** questions. All questions carry equal marks and the distribution of the marks for each question is given.
3. Write your answers in the answer booklet provided.

QUESTION 1

Tyco International has operations in over 100 countries and claims to be the world's largest manufacturer and servicer of electrical and electronic components; the largest designer and maker of undersea telecommunications systems; the larger maker of fire protection systems and electronic security services; the largest maker of specialty valves; and a major player in the disposable medical products, plastics, and adhesives markets. Since 1986, Tyco has claimed over 40 major acquisitions as well as many minor acquisitions.

Kozlowski, the Chief Executive Officer of Tyco was the main actor in the financial troubles and legal battles in Tyco. Kozlowski was the main recipient of the money stolen from Tyco. In addition, he was the main influential person who persuaded other top-ranking Tyco officers and lower ranking employees to get involved and to keep silent to cover up for Kozlowski's illegal activities. This case shows that extensive involvement of Kozlowski and other leaders in unethical and illegal activities brought Tyco down.

The complications in Tyco's case involved people other than Kozlowski. Kozlowski recruited the support of other high-ranking officers in the organization. He also convinced some lower ranking employees to keep their silence in exchange for financial benefits. Also, Kozlowski convinced one of the board members to keep silent about the illegal financial transactions on the mansion Tyco paid for the benefit of Kozlowski and his wife. In exchange, the board member received financial benefits.

The audit firm, PricewaterhouseCoopers who was responsible for auditing the financial reports of Tyco, was questioned by shareholders to identify Kozlowski's illegal financial transactions. Kozlowski's unethical business practice continued and became extensive. Tyco used improper accounting practice for booking bonuses against reserve accounts, instead of expensing them. For example, the company expensed only \$45 million of a special unapproved \$96 million bonus. The remainder was charged to unrelated reserve accounts, including a \$41 million offset to accrued federal income tax. PwC was aware of the improper accounting techniques used to hide the bonus payments. Ultimately PwC had to pay \$225 million to disgruntled shareholders in Tyco to settle claims for its failure to detect massive accounting frauds.

Kozlowski tried to avoid paying sales taxes for his art purchases because doing so would raise red flags for authorities. Sales taxes create formal records of financial transactions. In Tyco's case, the sales taxes amounted to millions because the purchased art items were expensive. It would have been easier for authorities to detect Kozlowski's illegal financial transactions because it was unusual for Tyco officers like Kozlowski to make such big purchases in a small amount of time.

The concept of 'commingling of assets' in Tyco's case refers to the adoption of the view that the assets of an employee are similar to the assets of the company. 'Commingling of assets' occurred when Kozlowski considered the assets of Tyco as his own personal assets. Kozlowski used Tyco's funds to pay for his personal expenses. He used Tyco's money to pay for his second wife's birthday party. He also used Tyco's money to cover the costs of properties he purchased. He used the company's money to purchase household items and art

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pieces for his personal use. Commingling of assets made it easy for Kozlowski to use the company's assets for personal needs. The company had programs that enabled Kozlowski to unethically use assets for personal needs. Kozlowski's use of Tyco's money was not just mere stealing of funds. It was also an exploitation of the weakness of the financial loopholes in the firm at the time of his leadership.

It would have been possible for the board of directors to see the adjustments taking place in programs at Tyco. This would have been so if the board of directors had appropriate mindsets and activity. Tyco's programs were a weakness in the organization. These programs provided benefits to officers and other employees. The financial programs were opportunities for Kozlowski's illegal financial transactions and unethical business practices.

The board of directors failed to examine these programs to evaluate their appropriateness. The directors should have identified the programs' weaknesses and loopholes, which Kozlowski and other officers exploited for their own personal benefit for years. The ineffectiveness of the board of directors in examining Tyco's programs enabled Kozlowski's unethical business practices.

One public investor once made serious comments on Tyco case scandal.

"Tyco's case shows that unethical practices may occur in different parts of an organization. Supposedly trusted leaders and executives with commendable background could exhibit unethical behavior and get involved in unethical practices. Even outsiders or third parties could get involved in these ethics issues. Codes of ethics and relevant assessments of the organization must include employees at all organizational levels, as well as significant third parties that interact in operations".

(Source: *Fraud Smart, KH Spencer Pickett, Business & Economics 2012*).

Required:

- a. Explain 2 (two) major ethical issues in Tyco's case. (8 marks)
- b. What is "commingling of assets" in Tyco's Case? How did Kozlowski used "commingling of assets" in Tyco? (5 marks)
- c. Was there any unethical auditing practice done by PWC? If yes, explain it. (3 marks)
- d. Briefly explain 3 (three) important functions of Board of Directors in today's environment? (9 marks)

[TOTAL 25 MARKS]

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QUESTION 2

In May of 1968, the Ford Motor Company, based upon a recommendation by then vice-president Lee Iacocca, decided to introduce a subcompact car and produce it domestically. In an effort to gain a large market share, the automobile was designed and developed on an accelerated schedule. During the first few years, sales of the Pinto were excellent, but there was trouble on the horizon.

In May 1972, Lily Gray was traveling with thirteen year old Richard Grimshaw in a 1972 Pinto when their car was struck by another car traveling approximately thirty miles per hour. The impact ignited a fire in the Pinto which killed Lily Gray and left Richard Grimshaw with devastating injuries. Six months following the controversial Grimshaw verdict, Ford was involved in yet another controversial case involving the Pinto. The automobile's fuel system design contributed (whether or not it was the sole cause is arguable) to the death of three women on November 10, 1972 when their car was hit by another vehicle traveling at a relatively low speed.

The controversy surrounding the Ford Pinto concerned the placement of the automobile's fuel tank. It was located behind the rear axle, instead of above it. This was initially done in an effort to create more trunk space. The problem with this design, which later became evident, was that it made the Pinto more vulnerable to a rear-end collision. This vulnerability was enhanced by other features of the car. The gas tank and the rear axle were separated by only nine inches. There were also bolts that were positioned in a manner that threatened the gas tank. Finally, the fuel filler pipe design resulted in a higher probability that it would disconnect from the tank in the event of an accident than usual, causing gas spillage that could lead to dangerous fires. The remedy available to Ford to overcome this design flaws is by installing a rubber blade in the gas tank. However Ford determined that the installation of rubber bladders was not cost-effective. Because of this design flaws, the Risk Committee of Ford became the center of public debate.

(Source: *The Ford Pinto case: The valuation of life as it applies to the negligence-efficiency argument, Law & Valuation, Professor Palmeter, 1999*).

Required:

- a. Based on 5-Questions Approach, explain whether it would be appropriate for Ford to install the rubber bladder. (12 marks)
- b. Briefly discuss 4 (four) roles of Risk Committee in ensuring the effectiveness of risk management in an organization. (8 marks)
- c. If Ford decided not to install the rubber bladder, briefly discuss this decision from the perspective of utilitarianism and deontology. (5 marks)

[TOTAL 25 MARKS]

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QUESTION 3

Your company has just been appointed as the new auditor of ACE Corporation (ACE). This had been an achievement for your company especially in this challenging business environment. Based on your review of the prior audited financial statements file, you concluded that the company had maintained a good set of records and accounts. No significant errors were found.

A week later, your subordinate checks the creditors section of the file. Based on prior records and supporting documents, there were no major changes for this year records. There was, however, a note from the audit senior stating that a large accrual had been included for taxes. There was an accrual of RM750,000 which was included in the accounts. It had been accrued in previous years. It was clear that the company had not made any payment of taxes for a period of 6 years. There was no consent letter with regard to this issue from the predecessor auditor. You had contacted the accountant of ACE and he ensured that the expense had been properly reflected in the accounts. You made a note of this and plan to talk to the board of directors of ACE during client's meeting.

Required:

- a. Based on the above situation, briefly explain 3 (three) ethical issues that will influence your decision? Suggest 3 (three) key parties who can influence, or will be affected by your decision? (9 marks)
- b. Briefly discuss 4 (four) fundamental ethical principles that are most applicable in this case. (8 marks)
- c. Briefly explain 4 (four) categories of threats that may affect compliance with fundamental ethical principle among professional accountants. (8 marks)

[TOTAL 25 MARKS]

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QUESTION 4

- a. Explain with justifications why is it significant in today's changing environment, for the clients of professional accountants to be ethical? (3 marks)
- b. Briefly explain the 3 (three) perspectives of Velasquez Approach. (9 marks)
- c. You are a trainee accountant and you have been told by your manager to complete a complicated reconciliation work for a client within 2 days and you are due to go for leave. You feel that you are not sufficiently experienced to complete the work alone. You would need additional supervision to complete it to the required standard, and your manager appears unable to offer the necessary support.

Based on the above situation, discuss 8 (eight) possible course of action that you should take. (8 marks)

- d. In accordance to MIA By-Laws, list 2 (two) provisions for members in charging their clients. (5 marks)

[TOTAL 25 MARKS]

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